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No. 89 -

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1989

ROCKFORD MEMORIAL CORPORATION AND SWEDISHAMERICAN CORPORATION,

Petitioners,

v.

UNITED STATES OF AMERICA,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

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July 2, 1990

QUESTIONS PRESENTED

1. Whether this Court's decisions in *Minnesota Mining & Mfg. Co. v. New Jersey Wood Finishing Co.*, 381 U.S. 311 (1965), and *United States v. Penn-Olin Chemical Co.*, 378 U.S. 158 (1964), that section 1 of the Sherman Act is a more demanding standard than section 7 of the Clayton Act, are no longer valid.

2. Whether the merger of two hospitals is properly gauged in narrow, local markets when those markets do not meet the legal tests of *Brown Shoe Co. v. United States*, 370 U.S. 294 (1962), and *Tampa Electric Co. v. Nashville Coal Co.*, 365 U.S. 320 (1961).

3. Whether the lower courts erred in finding a merger presumptively unlawful based on concentration ratios, instead of investigating all relevant economic facts as required by *United States v. General Dynamics Corp.*, 415 U.S. 486 (1974).

LIST OF PARTIES

The parties to the proceedings below were petitioners Rockford Memorial Corporation and SwedishAmerican Corporation and respondent United States of America. Petitioners are not-for-profit, federally tax-exempt corporations controlling, respectively, Rockford Memorial Hospital and SwedishAmerican Hospital. Petitioners were defendants below.

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STATUTES INVOLVED

Section 1 of the Sherman Act (15 U.S.C. § 1), in pertinent part, provides as follows:

> Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several states, or with foreign nations, is declared to be illegal.

Section 7 of the Clayton Act (15 U.S.C. § 18) provides as follows:

> No person engaged in commerce or in any activity affecting commerce shall acquire, directly or indirectly, the whole or any part of the stock or other share capital and no person subject to the jurisdiction of the Federal Trade Commission shall acquire the whole or any part of the assets of another person engaged also in commerce or in any activity affecting commerce, where in any line of commerce or in any activity affecting commerce in any section of the country, the effect of such acquisition may be substantially to lessen competition, or to tend to create a monopoly.

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IN THE

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OPINIONS BELOW

The opinion of the United States Court of Appeals for the Seventh Circuit is reported at 898 F.2d 1278 and is reprinted in Appendix B, *infra.*

The memorandum opinion of the United States District Court for the Northern District of Illinois is reported at 717 F. Supp. 1251 and is reprinted in Appendix A, *infra.*

JURISDICTION

The judgment of the court of appeals was entered on April 3, 1990. The jurisdiction of this Court is invoked pursuant to 28 U.S.C §1254(1) (1982).

The opinions of the United States Court of Appeals for the Fourth Circuit (which was not published) and the United States District Court for the Western District of Virginia, which conflict with the Seventh Circuit's opinion here, are reprinted in the Appendices B, C and E, *infra*.

STATEMENT OF THE CASE

I. Procedural History

On June 1, 1988, the United States of America brought two unprecedented actions seeking to block the mergers of not-for-profit organizations operating hospitals. In this action the government sought to enjoin petitioners Rockford Memorial Corporation and SwedishAmerican Corporation, which operate hospitals located in Rockford, Illinois, from merging. In the companion case, the government sought to enjoin two hospitals from merging in Roanoke, Virginia. The virtually identical complaints alleged violations of both section 7 of the Clayton Act and section 1 of the Sherman Act. These actions marked the first time in the ninety-eight year history of the Sherman Act and the seventy-four year history of the Clayton Act that the antitrust laws had been invoked to stop the combination of two not-for-profit institutions.

The district court in the Roanoke case, which was decided first, concluded that section 7 of the Clayton Act did not apply to the merger of not-for-profit entities, and that the merger did not violate the more demanding rules of section 1 of the Sherman Act. *United States v. Carilion Health System*, No. 88-0249-R (order granting motion to dismiss)(W.D. Va. Sept. 30, 1988); *United States v. Carilion Health System*, 707 F. Supp. 840 (W.D. Va. Feb. 13, 1989). The Fourth Circuit affirmed both rulings. *United States v. Carilion Health System*, 892 F.2d 1042 [unpublished opinion], 1989-2 Trade Cas. (CCH) ¶68,859 (4th Cir. Nov. 29, 1989); App. E. In contrast, the district court here ruled that section 7 did apply to not-for-profit mergers, thereby obviating the need to consider section 1. *United States v. Rockford Memorial Corp.*,

717 F. Supp. 1251, 1252-58 (N.D. Ill. Feb. 23, 1989). The court then found a violation of section 7 and enjoined the merger. *Rockford Memorial*, 717 F. Supp. at 1291-92. The Seventh Circuit, openly disagreeing with the Fourth Circuit, affirmed. *United States v. Rockford Memorial*, 898 F.2d 1278 (7th Cir. April 3, 1990).

II. The Contrasting Rulings Below

A. Section 7 and Not-For-Profits

In the Roanoke case, the district court granted a motion to dismiss the Clayton Act claim. It held that section 7 of the Clayton Act could not be applied to not-for-profit hospitals because (1) not-for-profits cannot issue stock and thus cannot be reached by the stock acquisition clause of section 7 and (2) not-for-profits are not subject to the jurisdiction of the Federal Trade Commission, pursuant to Section 4 of the Federal Trade Commission Act, 15 U.S.C. § 44, and thus cannot be reached by the asset acquisition clause. *Carilion Health System*, No. 88-0249-R (order granting motion to dismiss) (W.D. Va. Sept. 30, 1988); motion to reconsider denied, 707 F. Supp. 840, 841 n. 1 (W.D. Va. 1989).

In the Rockford case, the district court held that section 7 of the Clayton Act applied to not-for-profit institutions, relying on an expansive reading of *United States v. Philadelphia National Bank*, 374 U.S. 321 (1963). *Rockford Memorial*, 717 F. Supp. at 1253-55. On February 23, 1989, it found that the merger violated section 7 and entered an injunction. *Id.* at 1291-92. The district court never reached the government's claim under section 1 of the Sherman Act. *Id.* at 1292 n. 22.

The Seventh Circuit held that the district court's application of section 7 to the not-for-profits was wrong. *Rockford Memorial*, 898 F.2d 1278, 1281 (7th Cir. 1990). It nonetheless affirmed the injunction under section 1 of the Sherman Act, despite the fact that the district court made no findings on the section 1 claim. 898 F.2d at 1286. The court of appeals

reasoned that section 7 and section 1 actually present the same standard of liability and that two prior decisions of this Court were "old" and no longer valid:

> We doubt whether there is a substantive difference today between the standard for judging the lawfulness of a merger challenged under section 1 of the Sherman Act and the standard for judging the same merger challenged under section 7 of the Clayton Act. It is true that the operative language of the two provisions is different and that some of the old decisions (old by antitrust standards anyway) speak as if that should make a difference. E.g., *Minnesota Mining & Mfg. Co. v. New Jersey Wood Finishing Co.*, 381 U.S. 311, 323 (1965); *United States v. Penn-Olin Chemical Co.*, 378 U.S. 158 170-71 (1964). A transaction violates section 1 of the Sherman Act if it restrains trade; it violates the Clayton Act if its effect may be substantially to lessen competition. But both statutory formulas require, and have received, judicial interpretation; and the interpretations have, after three quarters of a century, converged.

Rockford Memorial, 898 F.2d at 1281-82. The court gave no weight at all to the earlier Fourth Circuit opinion. *Id.* at 1286.

B. The Market Analysis

The courts below found that the Rockford merger would reduce competition substantially in a product market described as acute inpatient care and a geographic market effectively limited to two and three-quarters Illinois counties — Winnebago and most of Boone, the northeast part of Ogle and small fractional pieces from McHenry, DeKalb and Stephenson Counties. Frankly conceding that these "markets" were flawed, the court of appeals approved the markets as defined by the district court without confronting the legal requirements for market definition. *Rockford Memorial*, 898 F.2d at 1284-85.

1. *The Product Market*

At least since this Court's decision in *Brown Shoe Co. v. United States*, 370 U.S. 294 (1962), product market definition has required an examination of reasonable interchangeability of use and cross elasticity of demand. The product market in Rockford — acute inpatient care — disregarded this test. The district court made extensive findings of fact that outpatient care:

- was a functional substitute for inpatient care for an increasing number of medical conditions[1]
- was provided by the same equipment and personnel as inpatient care;
- and was increasingly sought when inpatient treatment prices increased.

Rockford Memorial, 717 F. Supp. at 1296-97. Nevertheless, the court failed to understand the legal significance of those facts.

The court of appeals attempted to cure the legal omission by arguing that interchangeability was lacking. Certain acute inpatient care procedures (such as transplant surgery), it noted, can only be provided by hospitals. *Rockford Memorial*, 898 F.2d at 1284. As to these, the court speculated that "[h]ospitals can and *do* distinguish between the patient who wants a coronary bypass" [emphasis supplied] and other patients to "charge the former a higher price." *Id.* However, the government introduced no evidence of such price discrimination.

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[1] The record showed the following procedures were available on either an outpatient or inpatient basis: chemotherapy; radiation oncology; cardiac catheterization; hernia surgery and treatment; cataract surgery; alternative birthing centers; MRI, CT scanning and ultrasound imaging; renal dialysis; gastroenterology; pre-admission testing; occupational therapy; general surgery; kidney and gall stone lithotripsy; substance abuse treatment; liver functioning and treatment; "extended" outpatient surgery; diagnostic imaging; cardiac rehabilitation; laboratory work; laser surgery on tonsils; laser surgery on uterine fibroids; antibiotic intravenous therapy; and physical therapy.

The district court in the Roanoke case had reached the opposite conclusion based on a more expansive market — a product market of other inpatient hospitals and "also various outpatient clinics." *Carilion*, 707 F. Supp. at 847. The key difference in these results was not factual but legal: one court, the Seventh Circuit, gave little weight to substitutability, and the other court, the Fourth Circuit, accorded similar facts greater weight.

2. *The Geographic Market*

With respect to the geographic market, the court of appeals recognized that the district court did not comply with this Court's requirements for determining a geographic market — the two-part test from *Tampa Electric Co. v. Nashville Coal Co.*, 365 U.S. 320 (1961), that requires courts, first, to determine the area where sales are made (here, where the merging hospitals get their patients) and, second, to determine the area to which the purchaser can practicably turn for supplies (here, where patients in that area alternatively can go for care). The court of appeals acknowledged that the district court only performed the first part of that test by determining the area from which the hospitals obtain most of their patients. It never performed the second part. It never asked where people within the first area could go for alternatives and thus never saw the competitors who exert their influence on hospital pricing in Rockford. The court of appeals excused this defect saying that while the district court's market was "imperfect," the government was not required to "make an airtight case." *Rockford Memorial*, 898 F.2d at 1285, 1286. The omission was a central one: by disregarding the *Tampa Electric* test, both the district court and the court of appeals misperceived and overstated the concentration in the market.

This legal error tainted the factual conclusions both at the district court level and before the Seventh Circuit. For example, the court of appeals thought it defied "common sense" because it was illogical to assume that Rockford residents would seek out "obscure hospitals in remote rural

areas."[2] But, by focusing on the fact that Rockford residents tended to stay in Rockford, the court of appeals ignored the fact that the Rockford hospitals *depended on attracting patients* from an area beyond the urban core — patients who could and do turn to other hospitals at any time. The district court found that "[a]pproximately twenty-five to thirty percent of the patients actually utilizing the Rockford hospitals come to these hospitals from beyond the government's proposed geographic market." *Rockford Memorial*, 717 F. Supp. at 1303 (FF 120). This entire population was disregarded.

In fact, the economic importance of distant patients is disproportionately great when tertiary care is considered.[3] 717 F. Supp. at 1266. The court of appeals in Rockford discounted tertiary care, stating:

> For highly exotic or highly elective hospital treatment, patients will sometimes travel long distances, of course. But, for the most part hospital services are local.

898 F.2d at 1284-85. The district court had found that "[t]o the extent that patients are coming to Rockford for tertiary care, their economic importance to the hospital is greater than their numbers alone might indicate." *Rockford Memorial*, 717 F. Supp. at 1303 (FF 125). The record showed that at

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[2] Actually, petitioners' proposed geographic market was based on empirical data - patient travel data collected by the United States Health Care Financing Administration as part of the Medicare payment process which tabulates, by zip code, the actual origin for all Medicare patients at every hospital and similar data for all patients compiled by the Illinois Hospital Association for all Illinois hospitals. This data was analyzed by applying the Elzinga-Hogarty test, a methodology which follows the *Tampa Electric* test, to arrive at petitioners' proposed market.

[3] Primary care involves the prevention and early detection of disease. Secondary care involves more sophisticated treatment such as cardiology. *Carilion*, 707 F. Supp. at 843. Tertiary care includes heart surgery, chemotherapy and services requiring more sophisticated equipment and specialization. *Id.* All three hospitals in Rockford offer substantial tertiary care. *Rockford Memorial*, 717 F. Supp. at 1293.

Rockford Memorial, for example, tertiary and special services programs accounted for only 14% of admissions but 37% of patient days and 44% of inpatient revenue. Tr. 1677-78.

Both lower courts recited supposedly high concentration figures for the resulting market. But, to arrive at their figure, they included the hospital in Beloit, Wisconsin which was *not* in the geographic market they defined. *Rockford Memorial*, 717 F. Supp. at 1275; 898 F.2d at 1284. This implicitly acknowledged the defects in their geographic markets. If the market stretches as far as Beloit, Wisconsin, however, it includes far more hospitals and the antitrust analysis looks much different.

The result in the Roanoke case was starkly different. The Fourth Circuit approved a geographic market consisting of *sixteen* counties and two additional cities, as to primary/secondary hospital care alone. *Carilion*, 707 F. Supp. at 842-44, 847-48. In considering tertiary care, that court found that the Roanoke hospitals competed in a market that included Charlottesville and Richmond, Virginia and Winston-Salem and Durham, North Carolina. *Id.* at 848.

In the end, the disregard of the legal test for ascertaining a relevant geographic market in the Rockford case, contrary to this Court's decisions and in conflict with other circuits, tainted the opinion below. Had the court followed *Tampa Electric*, the geographic market would have been drawn more broadly, and the apparent market share of the merged hospitals would have been far lower.[4]

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[4] The economist for the hospitals testified that the respective market shares for the defendants' ten county geographic market were as follows:

	Beds	Admissions	Patient Days
Rockford Memorial	14.3%	14.8%	17.1%
SwedishAmerican	14.2%	13.6%	15.7%
Combined	28.5%	28.4%	32.8%

DX 114; Tr. 1140.

C. Predicting An Injury to Competition

This supposed highly concentrated market alone justified the injunction as far as the court of appeals was concerned. Ignoring this Court's pivotal decision in *United States v. General Dynamics Corp.*, 415 U.S. 486 (1974), the court did not look beyond its own statistics on market share. It never examined the structure, history and probable future of the particular market as required by *Brown Shoe* and *General Dynamics*. Similarly, the court of appeals never even considered why uncompensated, community-based trustees of a not-for-profit entity, many of whom pay employee health insurance premiums, should be presumed likely to collude or otherwise act anticompetitively to injure consumers (i.e., themselves) in the future. *Cf. Matsushita Electric Industrial Co. Zenith Radio Corp.*, 475 U.S. 574 (1986). As *amicus* American Medical Association pointed out below, hospital competition in the future inevitably will occur between larger, regional centers because of the need for sufficient capital and patient volume to support advancing medical technology. Brief of *Amicus Curiae* American Medical Assoc. in Support of Defendants-Appellants, *Rockford Memorial*, 898 F.2d 1278 (7th Cir. 1990)(No. 89-1900).[5] This trend is a result of a tremendous decline in hospital admissions and inpatient days due, in large part, to government programs aimed at reducing inpatient care. The Rockford hospitals, like many hospitals nationally, were operating at approximately two-thirds of their capacity in the time frame when the merger was planned. *Rockford Memorial*, 717 F. Supp. at 1294-95.

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[5] Economies of scale are becoming critical to successful competition. It was telling that the unrefuted evidence showed that a third hospital in Rockford strenuously opposed the merger, no doubt fearing it would lose business. *Cf. Cargill, Inc. v. Monfort of Colorado, Inc.*, 479 U.S. 104 (1986).

Preparing for this shift to more regional competition was exactly what the Rockford hospitals were seeking to accomplish with their proposed merger. As Dr. Robert Henry, then president of SwedishAmerican Corporation, testified, summing up the goals of the Rockford hospitals in pursuing the merger:

> [F]ive years . . . ago . . . the aggregate budget for the three hospitals in this community was something in the neighborhood of $250,000,000 a year and that . . . $250,000,000 supported three open heart programs, three emergency rooms, three obstetrical units, three pediatric units, three administrations, three budgets for marketing and advertising and recruitment and malpractice and you name it.
>
> * * *
>
> 250 million dollars a year is an awful lot of money, and I think the proposal that we've got in its nascent form is designed to reduce unnecessary duplication, to combine resources, to enhance the quality of the existing programs, to add new programs that aren't already in existence. An example, perhaps, transplant surgery that isn't available in this town.
>
> * * *
>
> And I honestly believe that if we are allowed to do this, we will develop a regional referral center in northern and northwest Illinois and southern Wisconsin that will attract new business, create new jobs, and it will help put Rockford on the map, as far as health care services are concerned.

Tr. 1980, 2006-08. The district court in Rockford expressly recognized that the merger would provide these benefits. *Rockford Memorial*, 717 F. Supp. at 1291. Unless this Court grants the petition, hospitals and similar industries across the

country will face different legal regimes for functionally identical mergers, and in the Seventh Circuit a legal standard that disregards this Court's prior decisions.

REASONS FOR GRANTING THE WRIT.

I.

The Seventh Circuit's Decision That Section 1 Of The Sherman Act And Section 7 Of The Clayton Act "Today" Present The Same Standard For Judging The Legality Of A Merger Conflicts With Prior Decisions Of This Court And A Recent Decision Of The Sixth Circuit.

Without any hint that this Court no longer approves its prior decisions in *Minnesota Mining & Mfg. Co. v. New Jersey Wood Finishing Co.*, 381 U.S. 311 (1965) and *United States v. Penn-Olin Chemical Co.*, 378 U.S. 158 (1964), the Seventh Circuit has swept those decisions aside to proclaim that section 1 of the Sherman Act and section 7 of the Clayton Act are the same. This holding is contrary to the plain language of the two statutes, the legislative history, two prior decisions of this Court and the recent decision of the Sixth Circuit in *White Consolidated Industries, Inc. v. Whirlpool Corporation*, 781 F.2d 1224, 1228 (6th Cir. 1986).

A. Earlier Decisions Of The Supreme Court

In *Minnesota Mining*, the Court was confronted with the question whether a Sherman Act action was barred by the four-year statute of limitations. The limitations bar would not apply if the pendency of an earlier FTC proceeding under section 7 of the Clayton Act was found to be a prior government proceeding such that the Sherman Act action was based "in part on any matter complained of" in the prior government proceeding. The Court's decision acknowledged that the Clayton Act and Sherman Act require different burdens of proof, though it held that the private action was based "in part" on the prior governmental proceeding:

> It is true that the Commission's Clayton Act proceeding required proof only of a potential anticompetitive effect while the Sherman Act carries the more onerous burden of proof of an actual restraint . . .
>
> Minnesota Mining's claim seems to be that the crucial difference between the Commission and the New Jersey Wood proceedings is that the former alleges conduct that *may* substantially lessen competition while the latter asserts activity that has *actually* done so. We think that this is a distinction without a difference and does not deprive New Jersey Wood of the tolling effect of § 5(b). That clause provides for tolling as long as the private claim is based "in part on any matter complained of" in the government proceedings. The fact that New Jersey Wood claims that the same conduct has a greater anticompetitive effect does not make the conduct challenged any less a matter complained of in the government action. It merely requires it to meet a greater burden of proof as to the effect of the conspiracy before a Sherman Act claim can be sustained.

381 U.S. at 323-24 (emphasis in original).

In *United States v. Penn-Olin Chemical Co.*, 378 U.S. 158 (1964), the Court reviewed a government challenge to the joint venture of Pennsalt Chemicals Corporation and Olin Matheison Chemical Corporation to produce sodium chlorate. The government challenged the transaction under both section 7 of the Clayton Act and section 1 of the Sherman Act. The district court found no violation and dismissed the action. The Court reversed as to section 7 of the Clayton Act but affirmed as to section 1 of the Sherman Act. The basis for this decision was that the trial court had failed to recognize that the Clayton Act has a lower standard than the Sherman Act:

> The grand design of the original § 7, as to stock acquisitions, as well as the Celler-Kefauver Amendment, as to

> the acquisition of assets, was to arrest incipient threats to competition which the Sherman Act did not ordinarily reach. It follows that actual restraints need not be proved. The requirements of the amendment are satisfied when a "tendency" toward monopoly or the "reasonable likelihood" of a substantial lessening of competition in the relevant market is shown. Congress made it plain that the validity of such arrangements was to be gauged on a broader scale by using the words "may be substantially to lessen competition" which "indicate that its concern was with probabilities, not certainties."

378 U.S. at 170-71, citing *Brown Shoe Co. v. United States*, 370 U.S. at 323.

Neither *Penn-Olin* nor *Minnesota Mining* has been questioned by this Court. To the contrary, the Court cited *Minnesota Mining* with approval in its April 30, 1990 decision in *California v. American Stores Company*, U.S. , 110 S. Ct. 1853, 1860-61 (1990). In *American Stores*, this Court twice referred to the fact that the purpose of the Clayton Act was to establish a *more* expansive standard of liability:

> Section 7 itself creates a relatively expansive definition of antitrust liability: to show that a merger is unlawful, a plaintiff need only prove that its effect "*may be* substantially to lessen competition."
>
> * * *
>
> Section 7 of the Clayton Act made stock acquisitions of competing companies more vulnerable . . . .

110 S. Ct. at 1860, 1862 (emphasis in original).

Irrespective of whether the precise difference between "tending to substantially lessen competition" and "restraining trade" can be debated, there is no question that

the legal standard for proof of a violation has always been more demanding for section 1 of the Sherman Act.[6]

Thus, findings that the lower standards of section 7 of the Clayton Act have been satisfied cannot be converted, without more, into findings that section 1 has also been violated. Cf. *Penn-Olin*. The court of appeals fundamentally and radically changed the relationship between the two statutes in its effort to equate them. This judicial legislation urgently requires this Court's intervention. *See* Sup. Ct. R. 10.

B. The Plain Meaning And Legislative History

Apparently, the Seventh Circuit believed that giving effect to the literal meaning of the statutes would produce "absurd results." But, this is the very reasoning this Court rejected in *Hallstrom v. Tillamook County*, U.S. , 110 S. Ct. 304, 310 (1989). In *Hallstrom*, the Court noted, "[n]othing in the legislative history . . . militates against honoring the plain language . . . . Nor is this one of the 'rare cases [in which] the literal application of a statute will produce a result demonstrably at odds with the intentions of its

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[6] While the court of appeals cited the Areeda & Turner treatise to support its "convergence" view, perhaps the more germane and revealing reference to academic literature would have been to then Professor Posner's 1976 book "Antitrust Law" and his chapter entitled "Toward the Simplification of Antitrust Doctrine." In it he advocated the repeal of Section 7 of the Clayton Act because it created a different standard than Section 1 of the Sherman Act. R. Posner, Antitrust Law 212-14 (1976).

In the fourteen years since Professor Posner advocated this, neither Congress nor any federal court ever previously took him up on the suggestion that section 7 be repealed or interpreted to be the same as section 1. This is not like the situation in *Continental T.V., Inc. v. GTE Sylvania Inc.*, 433 U.S. 36, 47-48 (1977), where the Court noted that "[t]he great weight of scholarly opinion has been critical of the [Schwinn] decision . . . ." The Seventh Circuit is not leading a parade of critics claiming that *Minnesota Mining* and *Penn-Olin* were wrongly decided and are economically irrational.

drafters.' " *Id.*, citing *United States v. Ron Pair Enterprises, Inc.*, U.S. , 109 S. Ct. 1026, 1031 (1989). Here, the legislative history clearly militates *against* the Seventh Circuit's view. The Report of the Attorney General's National Committee To Study The Antitrust Laws (March 31, 1955) at 117, summarized the pertinent legislative intent as follows: "Though the intent of Congress in making these changes is in some ways imprecise, one clear object is to strike down some mergers beyond the reach of the Sherman Act. Thus, the Senate Report explains that the 'bill is not intended to revert to the Sherman Act test. The intent here . . . is to cope with monopolistic tendencies in their incipiency and well before they have attained such effects as would justify a Sherman Act proceeding.' "

Nor has Congress expressed any dissatisfaction with the view that the statutes incorporate different standards. In 1976, when Congress passed the Hart-Scott-Rodino Act, it recognized the two Acts as having different standards: "Unlike the Sherman Act, Section 7 of the Clayton Act was meant to deal with potential, probable monopolies — not actual, completed ones." H.R. Rep. No. 94-1373, 94th Cong., 2d Sess., *reprinted in* 1976 U.S. Code Cong. & Admin. News 2572, 2639.

C. Conflict In The Circuits

While the Seventh Circuit regarded the prior Supreme Court decisions to be "old" and no longer valid on the question of whether there is a substantive difference between section 1 and section 7 today, the Sixth Circuit, as recently as 1986, followed those prior decisions (and a decision in the Fifth Circuit) to hold that a district court did not need to evaluate a merger under section 1 of the Sherman Act because it had found no violation under section 7 of the Clayton Act:

> Finally, plaintiffs contend the district court failed to evaluate the transaction for violations of Section 1 of the

> Sherman Act. The district court did not address plaintiffs' claims that the transaction violated Section 1 of the Sherman Act because it had found no violation under the less stringent Clayton Act standards of proof. We find no error in the district court's analysis. In our view, the plaintiffs' failure to sustain proof of potential anticompetitive effects under Section 7 of the Clayton Act precludes them from successfully establishing proof of a conspiracy in restraint of trade under the more vigorous standard for Section 1 of the Sherman Act. *Minnesota Mining & Manufacturing Co. v. New Jersey Wood Finishing Co.*, 381 U.S. 311, 323, 85 S. Ct. 1473, 1479, 14 L.Ed.2d 405 (1965), *Domed Stadium Hotel, Inc. v. Holiday Inns, Inc.*, 732 F.2d 480, 486 (5th Cir. 1984).

White Consolidated Industries, Inc. v. Whirlpool Corporation, 781 F.2d 1224, 1228 (6th Cir. 1986).

This Court should issue a writ of certiorari to review the Seventh Circuit decision which conflicts with two prior decisions of this Court, a decision of the Sixth Circuit and misinterprets the plain language of the statutes in question.[7]

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[7] Implicit in petitioners' argument is the proposition that the merger is lawful if section 1 is the only applicable statute. This is so first because, as petitioners argued to both courts below, section 7 does not apply to not-for-profit mergers. *See United States v. Carilion Health System*, No. 88-0249-R (order granting motion to dismiss) (W.D. Va. Sept. 30, 1988). The suggestion by the court of appeals, in dictum below, that section 11 of the Clayton Act supplies jurisdiction over not-for-profit entities fails to recognize that this Court expressly rejected the suggestion that "subject to the jurisdiction of the Federal Trade Commission" in section 7 of the Clayton Act referred to section 11 of the same Act in *United States v. Philadelphia National Bank*, 374 U.S. 321 at 336 n. 11 (1963); *see also id.* at 344 n. 22. Also, the suggestion is contrary to the plain meaning of section 11 which speaks of "authority . . . where applicable." The grant of authority in section 11 to the Federal Trade Commission to enforce section 7 is in cases *where* its own *authority* is *applicable* — which must be determined by reference to the Federal Trade Commission Act, 15 U.S.C. §§ 44 and 45. Secondly, as Parts II and III below demonstrate, the merger was lawful even under section 7 standards.

II.
The Narrow, Local Markets Approved By The Seventh Circuit For Gauging The Legality Of The Merger Conflict With The Legal Tests For Market Definition Established By Prior Decisions Of This Court.

If the markets had been defined properly, it would have clearly shown no violation of section 7 of the Clayton Act (assuming *arguendo* it applies), and *a fortiori* no violation of section 1 of the Sherman Act. The Seventh Circuit's decision conflicts with the decision of the Fourth Circuit and departs from this Court's decisions in *Brown Shoe* and *Tampa Electric*.

A. The Product Market, Properly Defined, Included Outpatient Care.

This Court has held that the outer boundaries of the relevant product market are determined by "the reasonable interchangeability of use or the cross-elasticity of demand between the product itself and substitutes for it." *Brown Shoe*, 370 U.S. at 325. The record in this case — reflected in the district court's own findings — established that outpatient care is a functional substitute for a significant and growing amount of inpatient care and that the buyers of health care services — mostly third-party payers — are extremely price sensitive, increasing their demand for outpatient care in direct response to the increased cost of inpatient treatment. In coming to a product market definition that ignored outpatient care, the district court and the court of appeals did not follow the legal test for defining a product market as established by decisions of this Court.

The court of appeals did not examine the functional interchangeability or cross-elasticity of demand. Functional interchangeability measures the degree to which different products may be used for the same end purpose. While two products must be realistic substitutes, total fungibility is not

necessary. *United States v. Continental Can Co.*, 378 U.S. 441, 455-57 (1964); *United States v. Connecticut National Bank*, 418 U.S. 656, 662 (1974).

The Roanoke case and the Rockford case, though mergers in different parts of the country, presented the same product market definition question but yielded diametrically opposite results. The court in the Roanoke case was sensitive to the ways in which outpatient treatment was a functional substitute for inpatient treatment:

> Various witnesses agreed that some medical needs are treated exclusively on an outpatient basis, while others are treated only in a hospital. Most also agreed, however, that a significant number of problems could be treated either on an in or outpatient basis. Reasonable doctors differ as to when a problem must be treated in a hospital or when outpatient treatment is appropriate. Moreover, various insurance carriers, including Blue Cross and Blue Shield of Virginia, two of whose executives testified at trial, have restructured their reimbursement policies in recent years in order to encourage patients to use outpatient services, which are less expensive than inpatient care. Because patients or their doctors can choose to have problems treated either in a hospital or in an outpatient clinic or doctor's office in a significant number of cases, the court finds that certain clinics and other providers of outpatient services compete with the defendants' hospitals to treat various medical needs.

Carilion, 707 F. Supp. at 844-45. The court in the Rockford case made findings reflecting the same competition. *Rockford Memorial*, 717 F. Supp. at 1296, 1297 (FF 40-52).

The court in the Roanoke case concluded that this competition required including outpatient services in the market. *Carilion*, 707 F. Supp. at 847. The Fourth Circuit approved. *Carilion*, 1989-2 Trade Cas. (CCH) at 62,515.

The court in the Rockford case, however, came to the opposite conclusion reasoning that "only an acute care hospital can provide the unique combinations of services which an acute care patient must have." *Rockford Memorial*, 717 F. Supp. at 1261.

The Seventh Circuit approved this result speculating that hospitals "can and *do*" distinguish between patients wanting more complicated inpatient services from others to charge the former higher prices. *Rockford Memorial*, 898 F.2d at 1284 (emphasis supplied). But, the government introduced no evidence to show that the bundle of charges that make up a hospital bill — room charges, lab fees, medicine, diagnostic imaging, etc. — varied one iota in their prices depending on the acuity of the patient's condition.

If outpatient services had been included in the product market, the resulting concentration ratios would have dropped dramatically. Whether outpatient services are properly part of a hospital's product market for purposes of antitrust analysis is a question facing hospitals throughout the United States considering mergers or joint ventures.

The Seventh Circuit's holding on the proper product market for determining the legality of this hospital merger directly conflicts with the result in the Fourth Circuit. It is also an extreme departure from product market determinations in other circuits that have followed the test of reasonable interchangeability and cross elasticity of demand. *See, e.g., Thurman Industries, Inc. v. Pay 'N Pak Store, Inc.*, 875 F.2d 1369 (9th Cir. 1989); *United States v. Syufy Industries*, 712 F. Supp. 1386 (N.D. Cal. 1989), *aff'd*, 1990 U.S. App. Lexis 7396 (9th Cir. 1990); *United States v. Baker Hughes, Inc.*, 731 F. Supp. 3 (D.D.C. 1990).

B. The Geographic Market Did Not Meet The Requirements Of Tampa Electric.

The court of appeals characterized the district court's geographic market as "imperfect". This was charitable. The

district court's geographic market never delineated the area in which the hospitals presently compete or, even more importantly, where they will be competing in the future. Mergers should not be enjoined based on fanciful markets that do not meet the market definition requirements of this Court.

Though not a merger case, this Court's decision in *Tampa Electric Co. v. Nashville Coal Co.*, 365 U.S. 320 (1961), is recognized as the seminal statement of how geographic markets are defined. The geographic market is "the area of effective competition . . . the market area in which the seller operates, and to which the purchaser can practicably turn for supplies." *Id.* at 327 (emphasis supplied). That determination requires two discrete inquiries to define a geographic market: (1) identifying the area in which the *sellers* operate, and (2) identifying the area to which the *buyers* can practicably turn for alternatives. *Id.* As a matter of law, both inquiries must be addressed. If geographic markets for antitrust enforcement purposes do not meet the rigors of this test, competitors will be inhibited from pursuing many beneficial transactions. *Cf. Business Electronics Corp. v. Sharp Electronics Corp.*, 485 U.S. 717 (1988); *Cargill, Inc. v. Monfort of Colorado, Inc., supra.* The Seventh Circuit decision conflicts with this requirement by approving a result where only one half of the test was met.

While the district court determined the area in which the hospitals operate ("the service area") (*Rockford Memorial*, 717 F. Supp. at 1273), it did not determine the market, the expanded area that includes where patients in the service area

can practicably turn for alternatives (*see id.* at 1274-75).[8] The court of appeals erred to hold that the district court's determination was not "clearly erroneous." The clearly erroneous rule cannot mask the legal error of failing to ask the right questions.

Hospitals today are under enormous pressures to become more efficient. Federal policies have changed 180 degrees. Previously, concern over access to health care services and facilities dominated government policies (the Hill Burton, Medicare and Medicaid programs) that reimbursed hospitals for the reasonable costs of providing care and encouraged the expansion of facilities. Since the late 1960s, cost containment has supplanted access as the principal concern of government policies. Now government programs pay hospitals based on prospectively determined rates for each of some 470 different types of cases, referred to as diagnosis

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[8] The district court criticized the market proposed by the government as not sufficiently accounting for the "large segment of immigrating patients" coming to the hospitals from beyond the government's proposed market. *Rockford Memorial*, 717 F. Supp. at 1266. The district court criticized defendants' application of the Elzinga-Hogarty test as "result oriented," and then attempted to design its own market applying Elzinga-Hogarty. *Id.* at 1267, 1270. In doing so, however, the district court misunderstood data which was "important" to its analysis. *Id.* at 1275. As shown by the court's own description, the district court mistakenly thought that DX 102 tabulated where residents in defendants' proposed ten county area go for hospital care. *Id.* at 1274.

This was wrong. Actually, as the title to the exhibit showed, DX 102 was a tabulation of hospital destinations for people within the *hospitals' consolidated service area*, a much smaller area. This was the area shown as the dotted zip codes in the district court's map (717 F. Supp. at 1274), an area that is less than half the size of the ten county area. *See* DX 102 and maps of the hospitals' service area and defendants' proposed geographic market (the ten county area) in the Appendix. App. F, G and H.

Because the court misunderstood the data, its perception of defendants' proposed geographic market analysis was skewed. Had it understood the data, its own market would have been far larger.

related groups (DRGs), regardless of the hospital's actual cost of providing the care. This system provides strong incentives to reduce the length of hospital stays, prevent unnecessary admissions and minimize unnecessary services. Inefficient hospitals will not survive.

In 1988, the American Hospital Association reported that 519 U.S. hospitals closed during the 1980-87 period. The trend continues unabated. Hospital trustees and administrators trying to grapple with the new dynamics of their industry are examining mergers, affiliations and joint ventures as natural strategic options. An overly restrictive geographic market standard, such as that approved by the Seventh Circuit, will skew antitrust analysis and condemn many transactions that would otherwise benefit consumers. The Seventh Circuit's geographic market decision conflicts with the Fourth Circuit, disregards the requirements of this Court's decision in *Tampa Electric* and wrongly decides an issue of federal law of importance to the entire health care industry, which encompasses approximately 11% of the gross national product.

If the Seventh Circuit decision is not reviewed, lower courts will be left with widely divergent market definition standards, making application of merger law totally unpredictable.

III.

Predicting An Injury To Competition Solely On The Basis Of Market Share And Concentration Statistics Conflicts With Prior Decisions Of This Court (1) That The Structure, History And Probable Future Of The Market Must Be Considered And (2) That Alleged Antitrust Violations Must Have A Sufficient Economic Rationale.

The court of appeals held that defendants' "immense shares in a reasonably defined market create a presumption of illegality." The court of appeals never looked any further.

Even recognizing that there would be some increase in concentration in a *correctly* defined market, this is not enough for liability even under Section 7. *Brown Shoe Co. v. United States*, 370 U.S. 294 (1962); *United States v. General Dynamics Corp.*, 415 U.S. 486 (1974). The Seventh Circuit's decision should be reviewed because it disregards this Court's prior decisions that statistics on market share and concentration are not conclusive (*Brown Shoe* and *General Dynamics*) and that antitrust violations should not be inferred where the supposed motive is economically irrational (*Matsushita Elec. Industrial Co. v. Zenith Corp.*, 475 U.S. 574 (1986)).

A. General Dynamics

General Dynamics required the court to determine how the supposed high market share of the hospitals related to their competitive strength in the hospital market of the future. Like all hospitals nationally, the Rockford hospitals face an eroding base of primary/secondary care. *Rockford Memorial*, 717 F. Supp. at 1296-98. Procedure after procedure is slipping away to outpatient providers such as surgicenters and doctors' clinics. The district court's findings make this clear. The district court differentiated inpatient care from outpatient care on the basis of the overnight stay: "At the core of these peculiar characteristics [that differentiate inpatient from outpatient care] is the hospital's ability to provide overnight care — no outpatient program can match this trait." *Id.* at 1260. However, the dynamics of this market is shown by the fact that even this basic distinction is disappearing. Illinois is in the process of adopting legislation that permits "Ambulatory Surgi-Centers" to treat patients on an overnight basis for three nights and, in some cases longer. H.B. 3587, 86th Leg., Gen. Sess., (1990). California and North Carolina have already enacted similar provisions. 1988 Cal. Legis. Serv. 2196 (West); N.C. Gen. Stat. § 131E-176 (1977) (amended 1984).

Strengthening tertiary care programs is the logical future for hospitals like the Rockford hospitals. Strengthening tertiary services obviously implicates a broader area in which patients have a wide array of alternatives.

Ironically, the district court and the court of appeals excluded Beloit Memorial, a twenty mile drive from the Rockford hospitals, from the "geographic market." However, the administrator of Beloit, who testified at trial, wrote a book called "Managing a Hospital Turnaround" in which he described how his hospital changed its tertiary referral arrangement to avoid losing patients to the Rockford hospitals:

> Beloit's hospital out-migration numbers made it clear that most local residents leaving the community for healthcare were going to one of three tertiary hospitals in a nearby northern Illinois city. Out-migration to those hospitals had a negative secondary effect on primary care business. For example, when a patient was referred to a competing tertiary hospital for heart surgery, neonatal care or other tertiary services, families tended to utilize the tertiary hospitals for primary care. As a result, the more tertiary business we lost, the more primary care business we lost too. The tertiary hospitals were only about a 20-minute drive from Beloit. It was obvious that people were willing to make the trip even for primary care because they perceived the quality of care was better.
>
> This discovery led us to make a strategic decision of great importance. I felt that the tertiary referral pattern to the three nearby Illinois hospitals needed to be redirected. A tertiary hospital approximately triple the distance was selected. The University of Wisconsin Hospital and Clinics, a major referral center for the midwest, was the obvious choice. The distance factor of 60 miles was great enough so that it was unlikely that primary care would be

> lost to the extent it had been to the nearby Illinois hospitals. Additionally, the medical capability of the University of Wisconsin Hospital and Clinics was superior to all three nearby tertiary hospitals.

Michael E. Rindler, Managing A Hospital Turnaround 156 (1987). The dynamics of the battle for tertiary care referrals caused the court in the Roanoke case not only to expand the geographic market (*Carilion*, 707 F. Supp. at 844, 848) but also to conclude that the merger would increase competition in the fight for tertiary services (*Id.* at 848, 849). The Fourth Circuit approved this result.

The Seventh Circuit decision invites courts to dispense with the inquiry into the relation of present market shares to competitive strength in the future. If *General Dynamics* still requires this inquiry, this decision should be reviewed.

B. The Failure To Address Motive

The court of appeals gave short shrift to the absence of an incentive to raise prices or act anticompetitively. Defendants never contended not-for-profits should be exempt generally from the antitrust laws, as the court of appeals suggested. Clearly, activities of not-for-profit entities have previously been found, after the fact, to have violated the Sherman Act. *National Collegiate Athletic Ass'n v. Board of Regents*, 468 U.S. 85 (1984). But the assumption the not-for-profit entity will do so in the future here is irrational and implausible. The defendants pointed out below that the trustees of the Rockford hospitals were closely aligned with consumers of hospital services. Many represented area employers who paid the cost of hospitalization for their employees and their families. The trustees were uncompensated. Unlike for-profit businesses, where decision-makers can profit through stock ownership or incentive compensation, the trustees and administrators of these (and, by definition, all other) not-for-profit hospitals cannot profit from any price decision they make. The court in the Roanoke case found that this absence of motive weighed

in favor of the merger being reasonable. The Seventh Circuit never supplied a plausible explanation for how an injury to competition could be predicted as likely to occur where the incentives for anticompetitive conduct were absent.

This Court has previously recognized that the absence of motive is important to the analysis of alleged antitrust violations. *NAACP v. Claiborne Hardware Co.*, 458 U.S. 886, 914-15 (1982). In *Allied Tube & Conduit Corp. v. Indian Head, Inc.*, 486 U.S. 492, 508-10 (1988), the Court explained *Claiborne Hardware* as follows: "Although the boycotters intended to inflict economic injury on the merchants, the boycott was not motivated by any desire to lessen competition or to reap economic benefits . . . and the boycotters were consumers who did not stand to profit financially from a lessening of competition in the boycotted market." Thus, the court of appeals failed to supply a plausible economic theory or rationale for why the not-for-profit hospitals could be expected to act anticompetitively in the future. *See also Monsanto Co. v. Spray-Rite Service Corp.*, 465 U.S. 752 (1984); *Cargill, Inc. v. Monfort of Colorado, Inc.*, *supra*; *Atlantic Richfield Co. v. U.S.A. Petroleum Co.*, U.S. , 110 S. Ct. 1884 (1990); *Apex Hosiery Co. v. Leader*, 310 U.S. 469, 493 (1940).

C. The Complaining Competitor

The court of appeals did not even consider the fact that a third large hospital located in Rockford, St. Anthony Medical Center, went to extraordinary lengths to oppose this merger. St. Anthony and its parent, the Sisters of the Third Order of St. Francis, admitted spending $49,800 on a secret campaign to block the merger through mid-May of 1988 alone.

St. Anthony is an aggressive competitor in the southern Wisconsin and Northern Illinois region.[9] St. Anthony

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[9] For example, St. Anthony considered that its geographic market for open heart surgery placed it in direct competition with Sherman Hospital in Elgin (i.e., beyond the court's geographic market).

retained two economists to assist in "evaluating" the competitive effect of the merger and articulating their findings to the government. The purpose of their effort was to block the merger as revealed in the following letters:

> The meeting with the Department of Justice went very well, from the standpoint of their willingness to be instructed in both the professional literature and appropriate analytical methodology. I suggest that you follow up as soon as possible by providing publications and responses to questions that were raised in the conversation.
>
> * * *
>
> Even though the government attorneys and economists seem willing to pursue MedPar data from the appropriate individual at HFCA (whose name Frank indicated he would supply), I expect that we will get much further if we can "spoon feed them."

DX 47.

> I would like to take this opportunity to thank [our economists] for their excellent work and outstanding presentations. Without taking anything away from Kevin's skillful and knowledgeable testimony, the work of our economists is probably the most important thing we have done to try to influence this enforcement decision. I have Richard Martin's promise to notify me as soon as possible of the Department's decision.

DX 49.

A rational competitor simply would not spend real resources to thwart a merger that was likely *to reduce competition*. Accord, *Matsushita Elec. Indust. Co. v. Zenith Radio Corp.*, 475 U.S. 574, 583 (1986) (conspiracy to raise price, though harmful to competition, actually *benefits* competitors). Had the Seventh Circuit considered this economic fact,

it might have recognized that the supposed increase in concentration here did not support a prediction that competition would be lessened substantially or that trade would be restrained.

The purpose of the antitrust laws is "the protection of *competition*, not *competitors*." *Cargill*, 479 U.S. 104, 107 S. Ct. at 489, quoting *Brown Shoe Co.*, 370 U.S. at 320 (emphasis in original). This Court's decision on May 14, 1990 in *Atlantic Richfield Co. v. USA Petroleum Co.*, U.S. 110 S. Ct. 1884, 1895 (1990), made it clear that a competitor that complains about a vertical, maximum price-fixing arrangement is in fact complaining about an arrangement that is pro-competitive. Here, St. Anthony's vociferous complaints about the merger indicate that the merger will produce a more efficient rival better able to compete.

This Court should grant review because the court of appeals failed to consider factors other than market share which show that there would not be an injury to competition. The Seventh Circuit's decision should be reviewed because it conflicts with this Court's decisions in *Brown Shoe* and *General Dynamics* which hold that market share statistics are not conclusive and with this Court's decision in *Matsushita* that antitrust violations cannot be premised on implausible economic theories. The decision conflicts with the Fourth Circuit where similar economic facts were considered.

CONCLUSION

In every important particular the Seventh Circuit's decision in the Rockford case conflicts with the Fourth Circuit's decision in the Roanoke case. This places the lower courts in a quandry as to whether the Clayton Act section 7 standard applies to not-for-profit hospital mergers, whether hospital mergers are appropriately gauged in narrow, local markets and whether the economic facts in the market place should be

considered or whether, instead, mergers are per se illegal at some level of increased concentration.

The Seventh Circuit's sweeping decision brushed aside numerous antitrust decisions of this Court. According to the Seventh Circuit's decision:

- *Minnesota Mining* and *Penn-Olin* are no longer valid today on the question of whether section 1 is a more demanding standard than section 7;
- *Tampa Electric*'s second question for defining a geographic market can be ignored;
- *Brown Shoe* and *General Dynamics* need not be followed and;
- *Matsushita's* requirement for a plausible economic rationale can be disregarded, when increases in concentration reach a certain level.

If the decision of the court of appeals is not reviewed, it will be unclear whether and to what extent this Court's prior decisions should be applied in merger cases in the future.

The serious questions petitioners raised below concerning the application of the antitrust laws to this proposed transaction have not been answered.[10] The answer to them will affect the delivery of health care for years to come. The

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[10] The court of appeals has used some strident language to dispose of petitioners' appeal points below: The geographic market alleged by petitioners was "ridiculous," defying "common sense," and "without any evidence." Petitioners' objection to the district court's geographic market was a "pot-shot." Petitioners' contentions about section 1 and section 7 were "word play." Petitioners' arguments about the absence of a sufficient motive to predict anticompetitive conduct, though delivered with "vigor and panache," were essentially frivolous we are told — just "conjecture" and "will o' the wisps."

But this is no answer to petitioners' arguments. As Henry Lee said, arguing for ratification of the Constitution in the Virginia Constitutional Convention of 1788, "Ridicule is not the test of truth." *See* Beveridge, The Life of John Marshall 423 (1916).

conflicting results in Rockford and Roanoke leave the hospital industry in disarray at a time when hospitals face increasing pressure rationally to reduce excess capacity and become more efficient. Mergers are a logical strategy for meeting the federal policies promoting reduced inpatient utilization, reduced capacity and greater efficiency. Yet the disparate results in Rockford and Roanoke and the absence of a reasoned approach to hospital market analysis stymies sound planning for the future of health care.

For these reasons, petitioners respectfully request this Court to grant their petition for a writ of certiorari.

Respectfully submitted.

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